



BEFORE THE STATE BOARD OF EQUALIZATION  
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of  
CLOYD C. HILLIS and CARRIE S. HILLIS)

Appearances:

For Appellant: Cloyd C. Hillis, in propria persona

For Respondent: **Harrison Harkins**, Associate Tax Counsel

O P I N I O N

This appeal is made pursuant to Section 19 of the Personal Income Tax Act (Chapter 329, Statutes of 1935, as amended) from the action of the Franchise Tax Commissioner in overruling the protest of Cloyd C. Hillis and Carrie S. Hillis to a proposed assessment of additional tax for the year ended December 31, 1935, in the amount of \$16.06,

On June 1, 1930, the Appellants purchased for their personal use certain residential property in Santa Ana, California, at the price of \$17,100, the price being paid by giving in exchange their former residence in Long Beach, California, and by assuming indebtedness against the property aggregating \$11,000. The Appellants occupied the Santa Ana house until September, 1934, when a change in the employment of the Appellant Cloyd C. Hillis required them to move elsewhere. Thereafter the property was rented, but the rents obtainable were insufficient to meet the required payments on the indebtedness, and in May of 1935 the Appellants deeded the property to the mortgagees in consideration for the cancellation of the indebtedness, on which the balance due at that time was approximately \$7,000.

As a result of this transaction the Appellants claim to have suffered a loss of some \$7,000. The proposed assessment has resulted from the refusal of the Commissioner to allow any **portio** of this amount as a deduction from gross income,

Section 8(d) of the Act allows the deduction of losses "incurred in any transaction entered into for profit." Under this provision one who sustains a loss **on the sale** of residential property which was purchased for **personal** use, but which was rented or otherwise used for **income-producing purposes** for a period immediately preceding the date of sale, may deduct the loss up to the amount by which the fair value of the property at the **time of** the conversion to income purposes exceeds the amount realized, subject to proper adjustments for depreciation, and **subject** also to the capital loss limitations provided by Section 7(e) of the Act; (Regulations Relating to the Personal Income Tax Act of 1935, Article 8(d)-1; Heiner v. Tindle, 276 U. S. 582.)

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The action of the Commissioner in disallowing the deduction was taken on the ground that there was no showing that the fair market value of the property at the time of its conversion to income purposes exceeded in the amount the \$7,000. indebtedness cancelled by the mortgagees. In our opinion, however, the Commissioner was not justified in disregarding the fact that the Appellant paid \$17,100 for the property in 1930. The relevancy of original cost as an indication of current value is well recognized. (Chicago Ry, Equipment Co. v. Blair, 20 F. 2d 10; State of Minnesota v. Federal Reserve Bank, 25 F. Supp. 14; Los Angeles Gas & Electric Corp. v. Railroad Commission, 289 U. S. 287, 306; Bonbright, Valuation of Property, p. 144.)

Likewise, the inability of an owner to find a buyer for his property does not mean that the property has no fair market value (Larkin v. Gage, 28 F. 2d 78; State of Minnesota v. Federal Reserve Bank, supra; Turnley v. Elizabeth, 76 N.J.L. 42, 68 Atl. 1094), nor do the terms "fair value" or "fair market value" refer to the price which could be obtained at a "forced sale?" (In re Crystal Ice & Fuel Co., 283 Fed. 1007; Nolte v. Hudson, Navigation Co., 8 F. 2d 859; Bonbright, Valuation of Property, p. 841.)

Without the allowance of any loss on the sale of the property the Appellants' net income for 1935 was \$1,606.20 in excess of their personal exemption and 'credit for dependents. It follows that allowing for the fact that under Section 7(e) only 60 per cent of the recognized loss may be taken into account in computing net income, in order for the Appellants to prevail it is necessary only that they establish that the fair value of the property in September, 1934, when it was converted to income purposes, was \$2,677, in excess of the amount realized,\*

In view of the \$17,100, purchase price paid in 1930, and in the absence of any other evidence as to the fair value of the property in September, 1934, when it was converted to income purposes, we believe there is ample justification for the conclusion that the value at that time was at least \$9,677., or \$2,677 in excess of the \$7,000 realized on the disposal of the property.

O R D E R

Pursuant to the views expressed in the opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED that the action of Chas. J. McColgan, Franchise Tax Commissioner, in overruling the protest of Cloyd C. Hillis and Carrie S. Hillis to a proposed assessment of additional tax in the amount of \$16.06 for the year ended December 31, 1935, be and the same is hereby reversed. Said ruling is hereby set aside and the said Commissioner is hereby directed to proceed in conformity with this order.

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\*  $\$1,606.20 \div .60 = \$2,677.00$

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Done at Sacramento, California, thfs 4th day of August, 1942,  
by the State Board of Equalization,

R. E. Collins, Chairman  
Wm. G. Bonelli, Member  
George R. Reilly) Member

ATTEST: Dixwell L. Pierce, Secretary